
Update on the Global Crisis: The Worst is Over, LAC Poised to Recover

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Chief Economist Office
Latin America and the Caribbean Region
The World Bank



Structure of Presentation

- The worst seems over, but fragilities remain
 - The nature of the incipient recovery
- How has LAC fared in comparative terms?
 - Recession in LAC and elsewhere
 - Growth collapse in LAC and elsewhere
 - Explaining the differences in growth collapse
- Looking ahead: much haziness in the horizon
 - Short-run recovery
 - Medium-term growth and rebalancing uncertainty

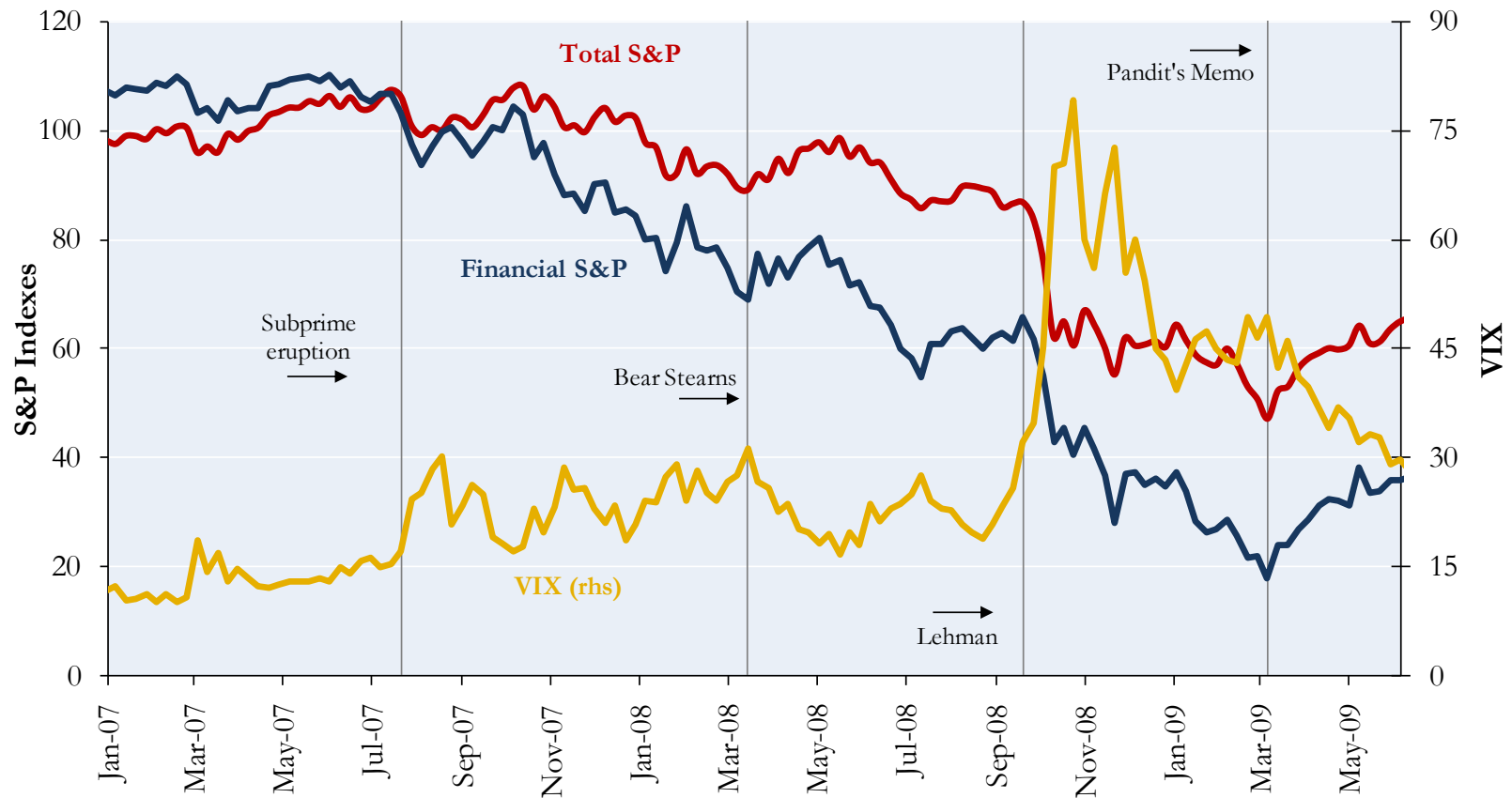
The Worst Seems Over But Fragilities Remain

Part 1

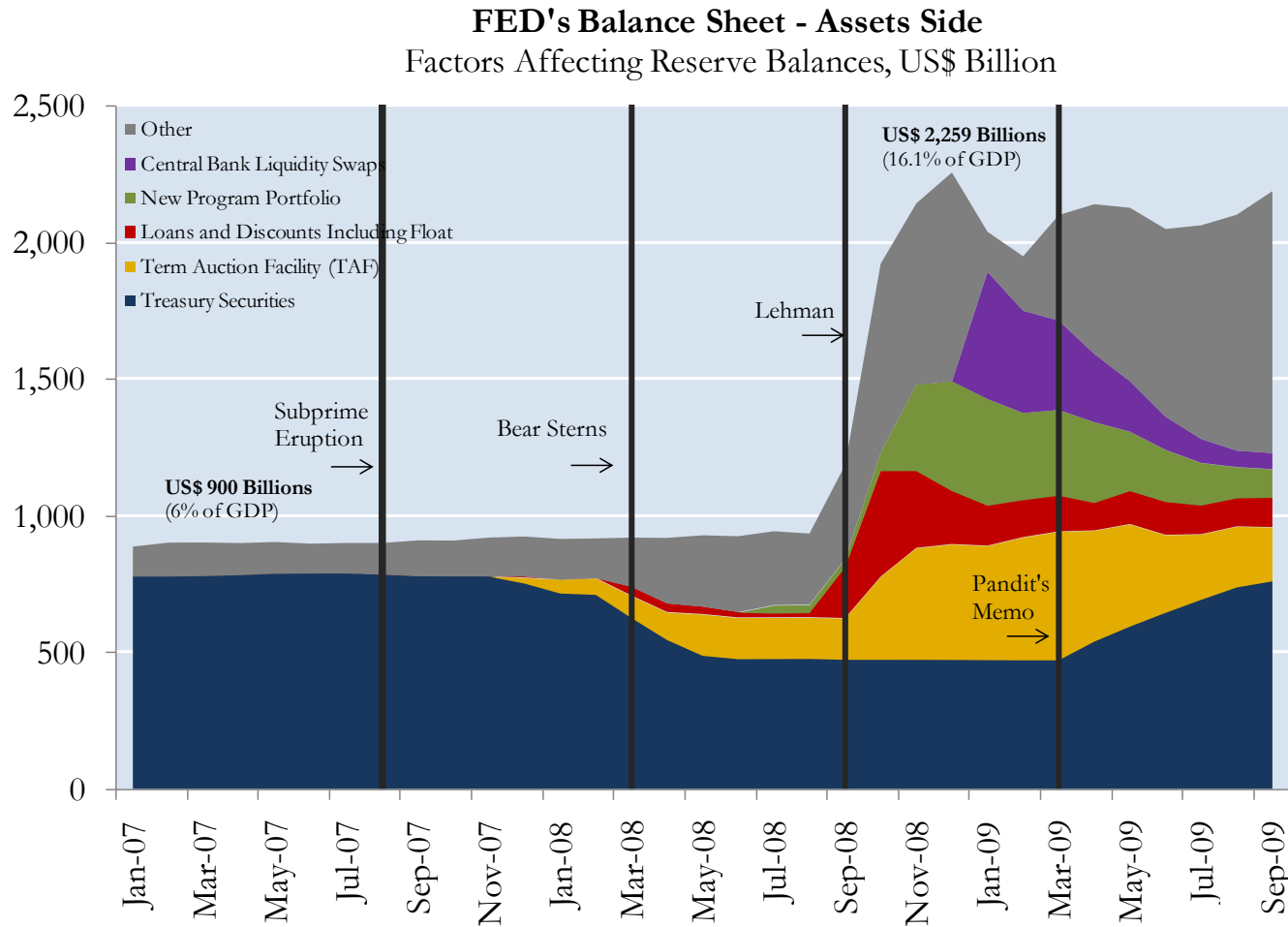
The catastrophic scenario was averted...

Standard & Poor's (Financial and Total Indexes) and VIX

Index number Aug-15-2007 = 100 (S&P indexes)

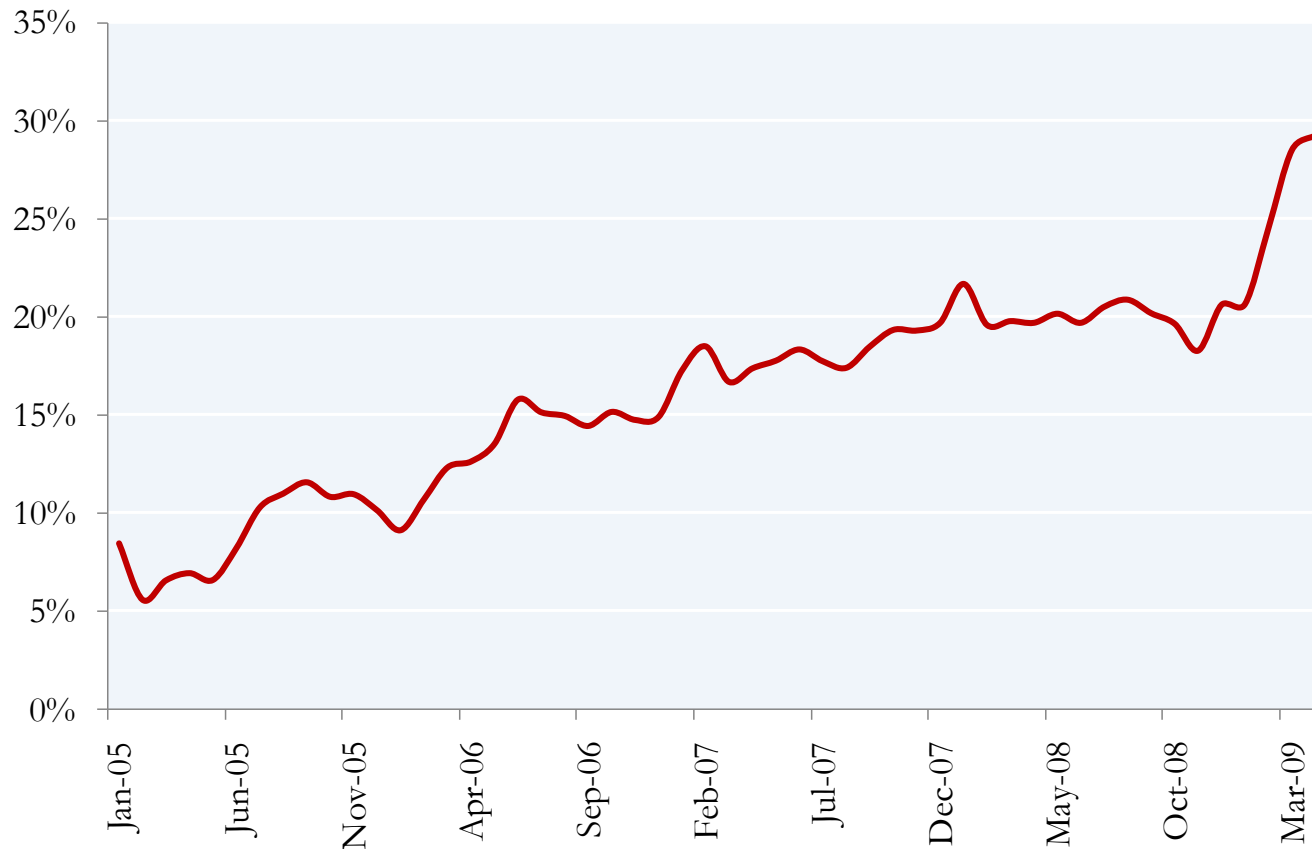


... thanks to bold risk absorption and countercyclical actions by central banks, led by the U.S. Fed ...



... and to substantial injections of fiscal and credit stimuli, including in China

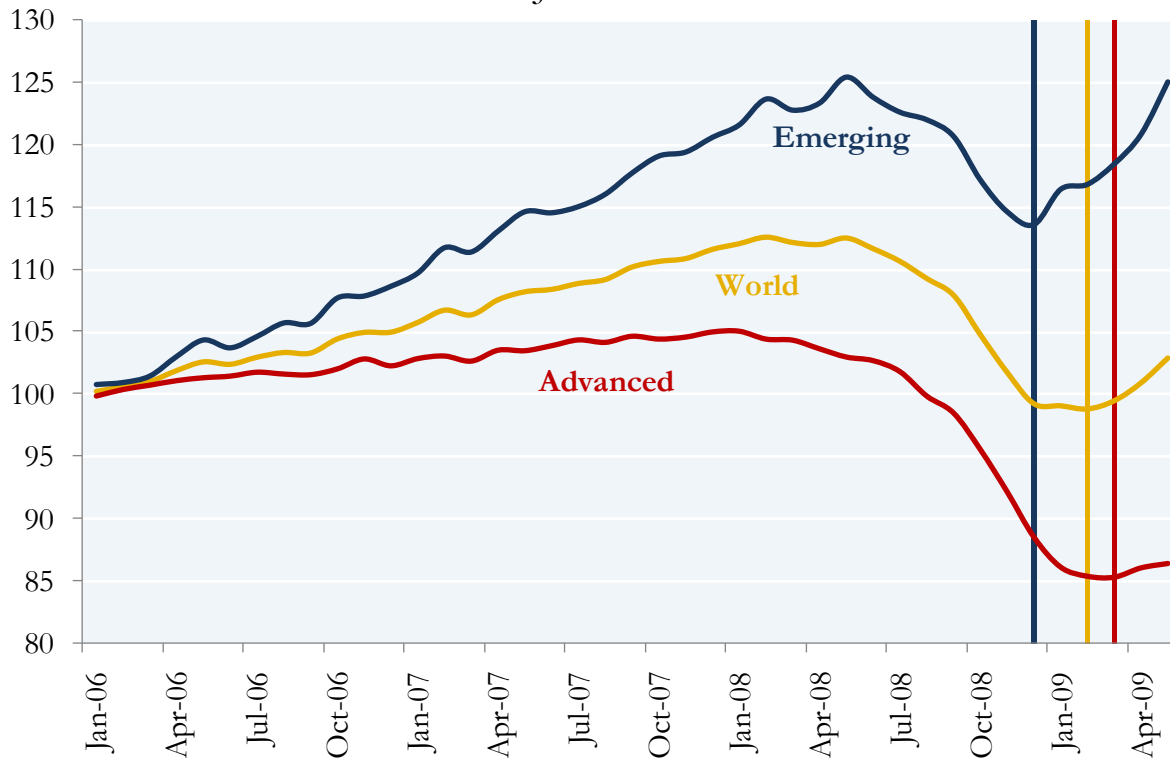
China: Real Private Domestic Credit
Annual Variation



The large emerging economies, including Brazil, are leading the world's recovery

World Industrial Production

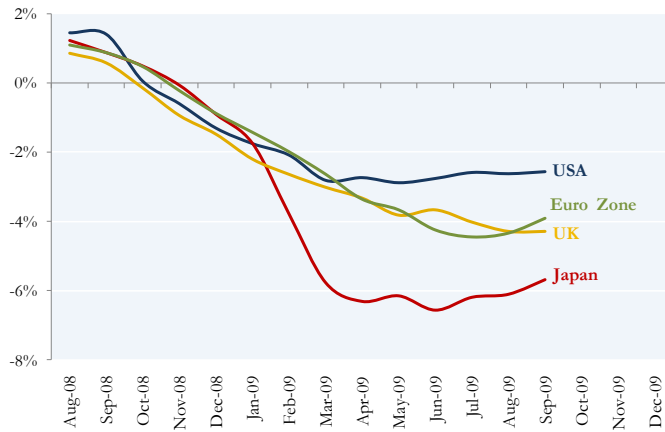
Index Jan/2006=100



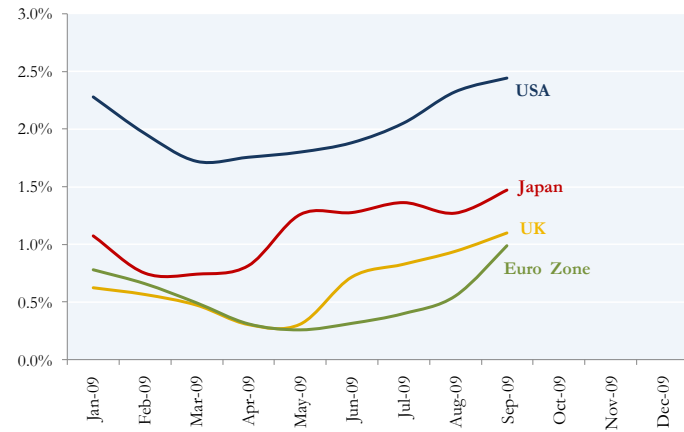
- The emerging economies with strongest recoveries include Brazil, China, India, Korea, Malaysia, Philippines and Thailand
- They represent 52% of emerging economies' GDP
- Industrial production for this group increased by 18% from January to June 2009

With surprises on the upside, growth forecasts for the center and the periphery are being revised upwards ...

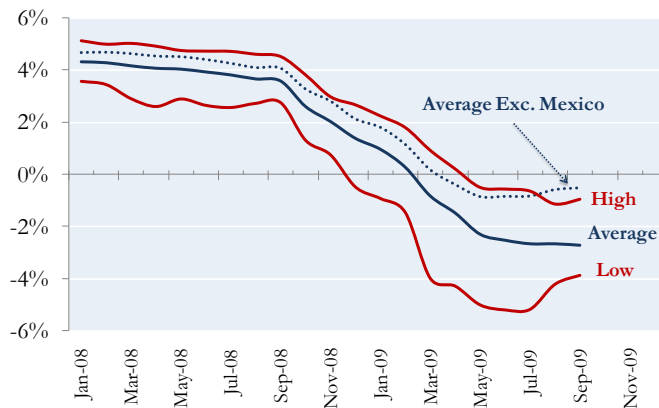
Developed Countries: 2009 Real GDP Growth Forecasts
Annual Growth Rate



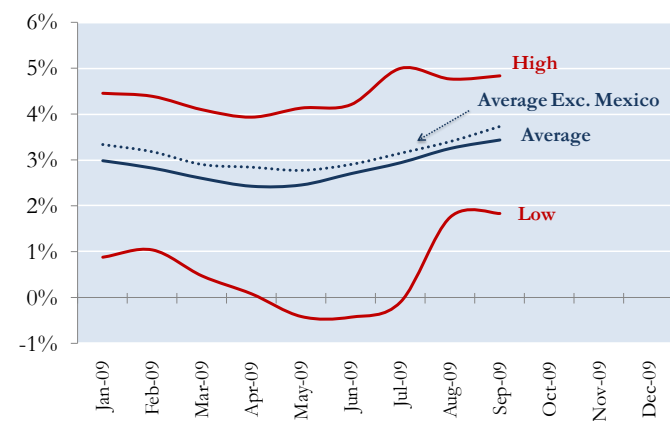
Developed Countries: 2010 Real GDP Growth Forecasts
Annual Growth Rate



LAC Countries: 2009 Real GDP Growth Forecasts
Annual Growth Rate

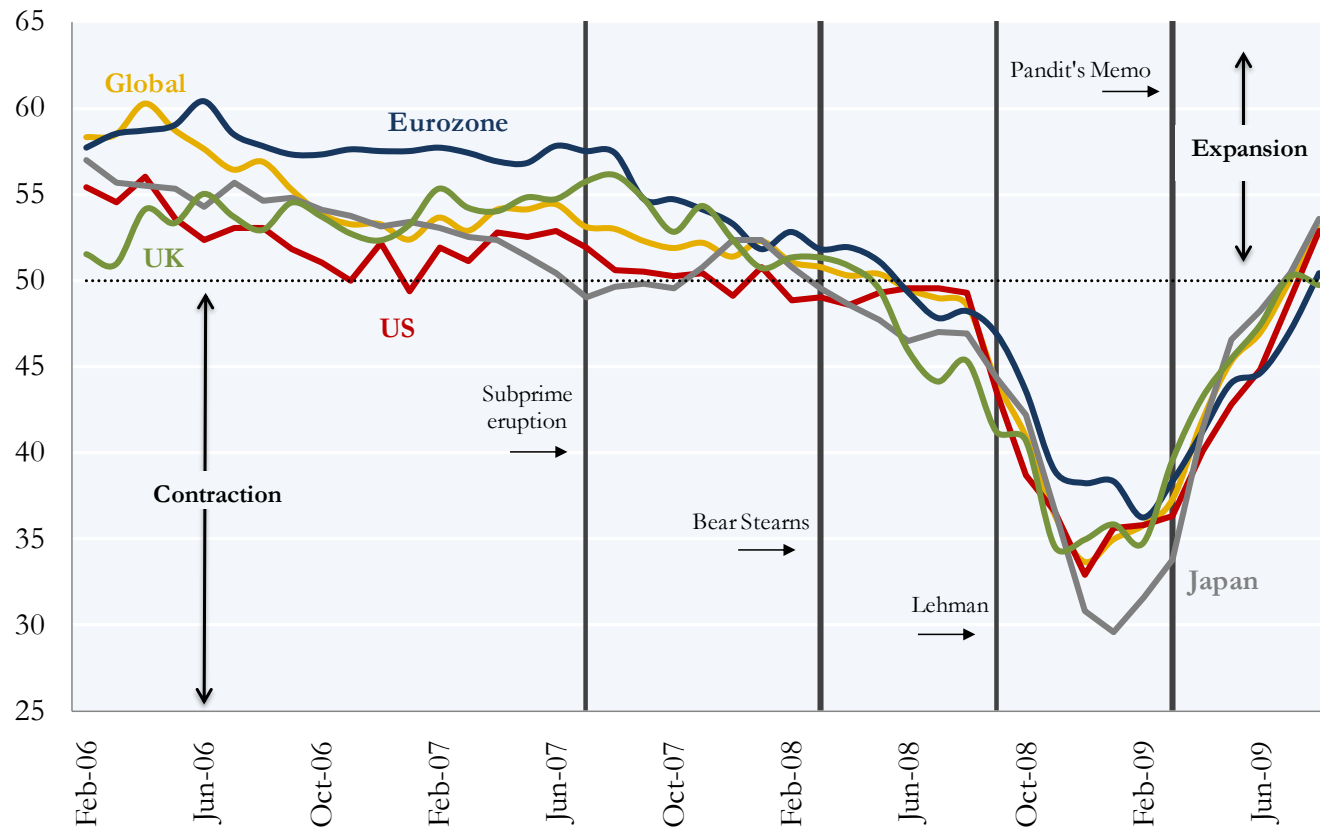


LAC Countries: 2009 Real GDP Growth Forecasts
Annual Growth Rate



However, the process of economic repair in rich countries is still incomplete ...

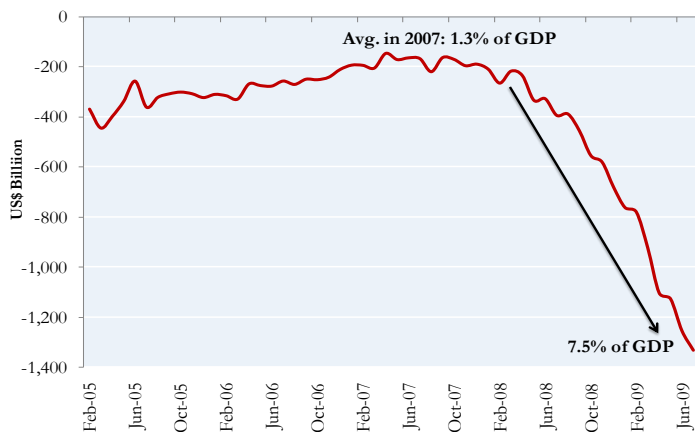
Developed Economies: Manufacturing PMI
Seasonally Adjusted



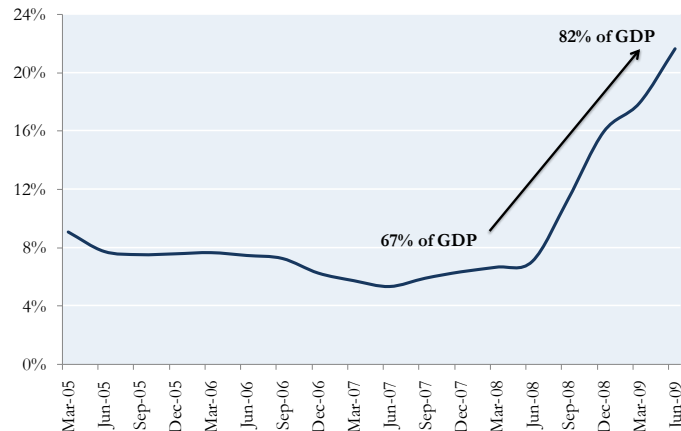
Manufacturing Purchasing Managers Index: assess business conditions in the manufacturing sector. A number above 50 indicates an expected increase of business conditions (expansion). A number below 50 indicates deterioration. Source: Bloomberg

... as the stimuli is most of the story so far behind the incipient recovery, especially in the US...

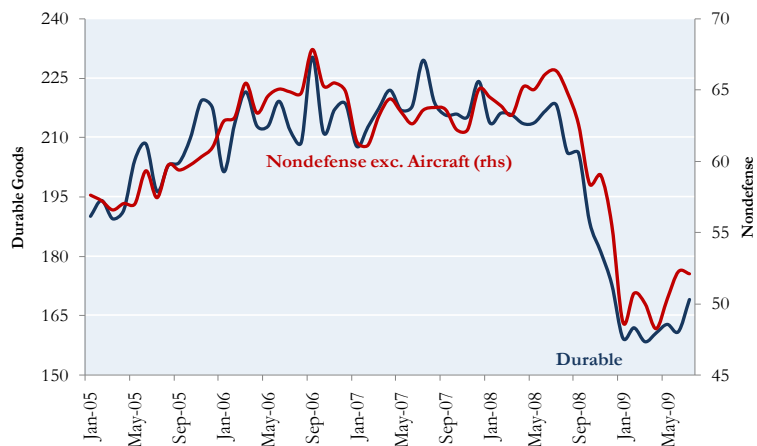
Budget Balance of Central Government
Accumulated in 12 Months



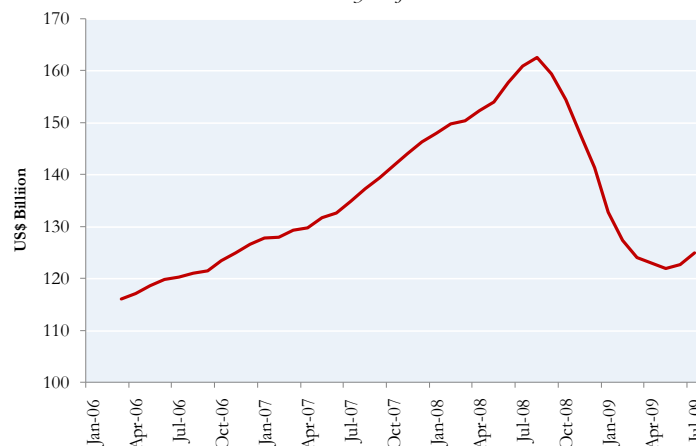
Gross Nominal Public Debt
Annual Variation



Manufacturers' New Orders
US\$ Billion, Seasonally Adjusted

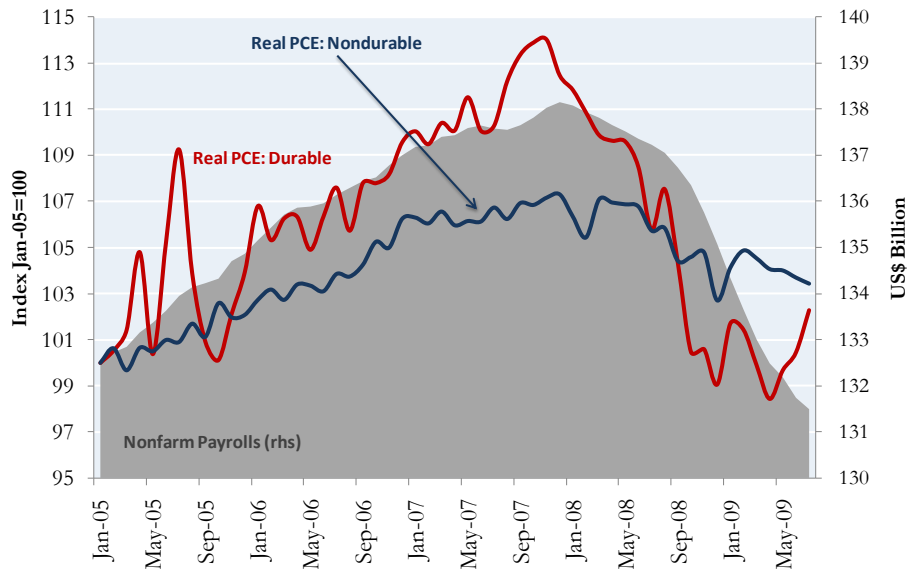


Exports of Goods and Services, BOP Basis
Seasonally Adjusted

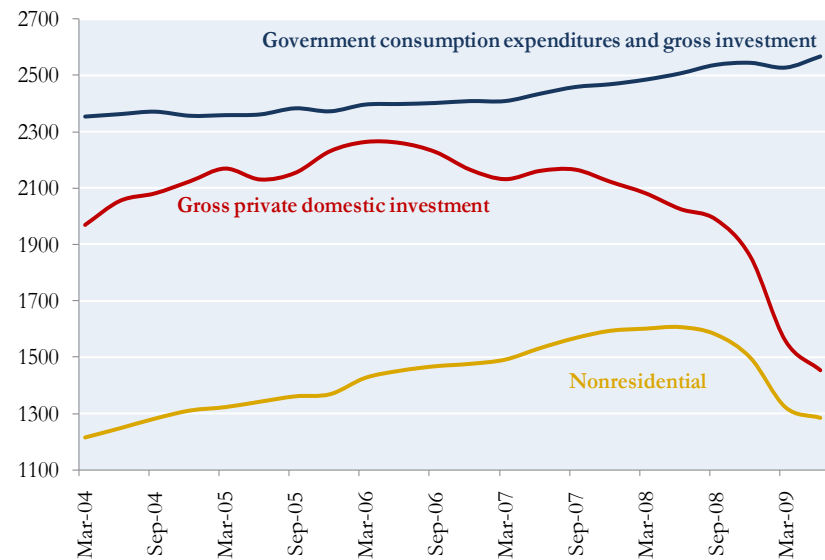


... and fragilities remain in labor markets and in private demand...

Nonfarm Payrolls and Personal Expenditures
Seasonally Adjusted

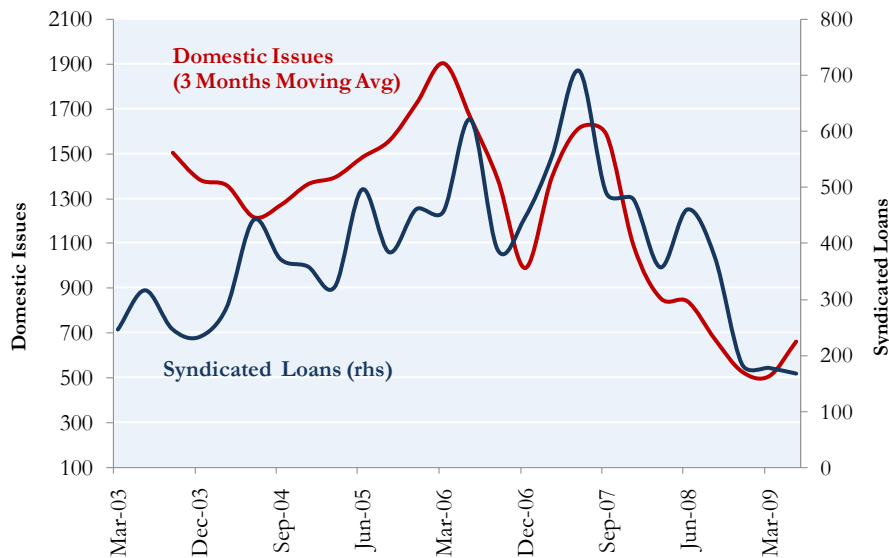


Investment
US\$ Billion

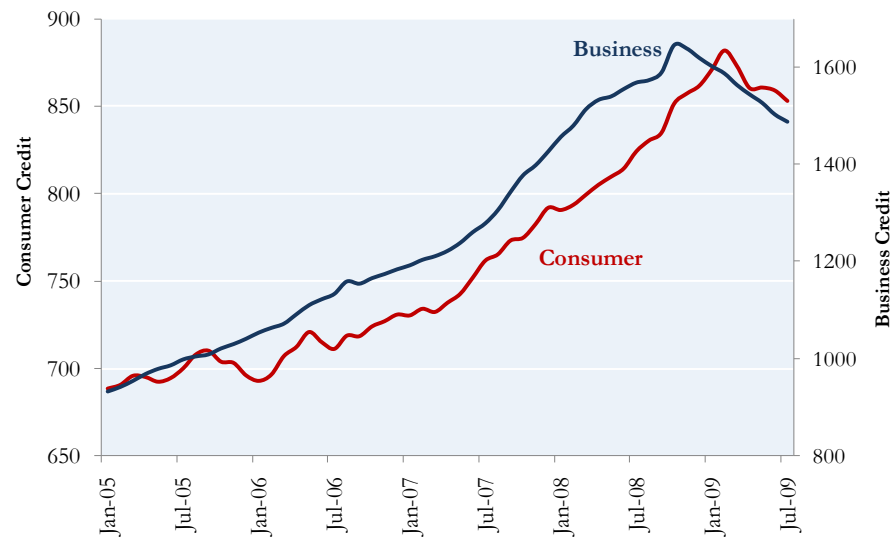


Also, domestic credit to households and firms remains sluggish

Capital Markets in the US
New Capital Raisings, US\$ Billion

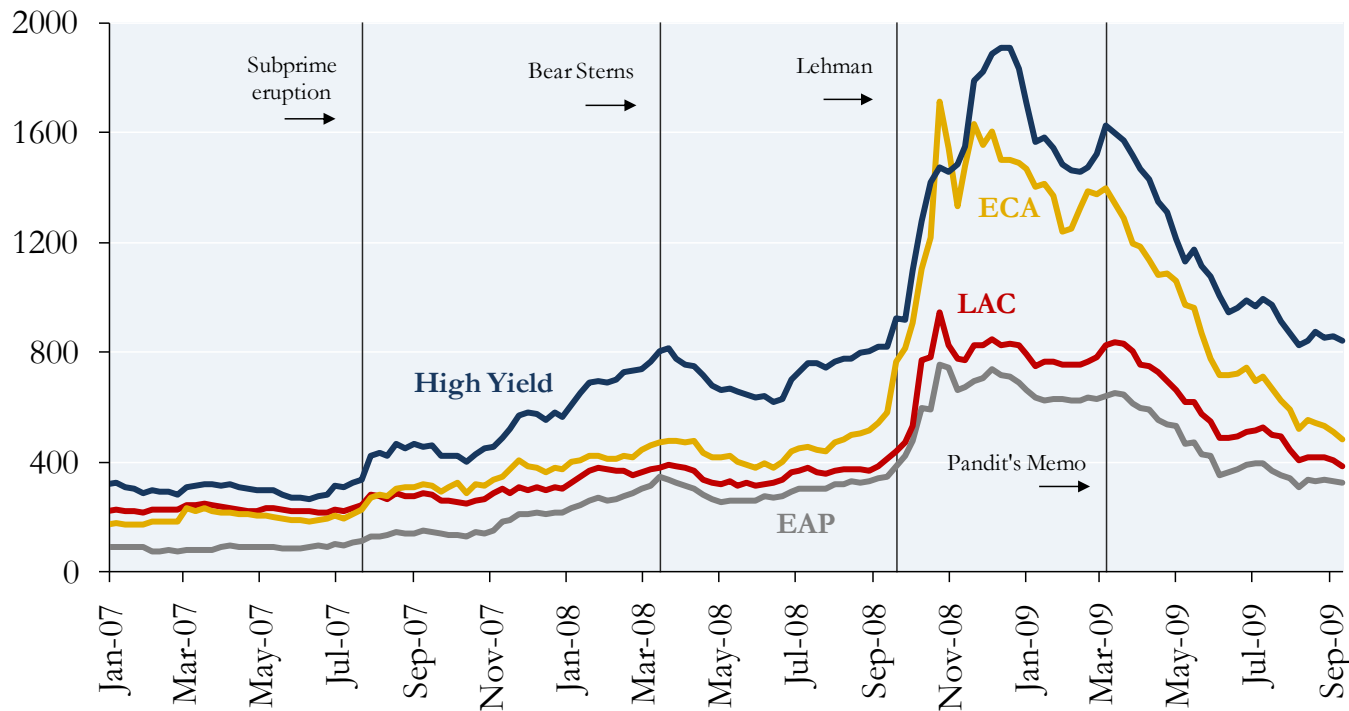


Private Credit in the US
US\$ Billions Seasonally Adjusted



External financial conditions have improved significantly for LAC and other emerging regions

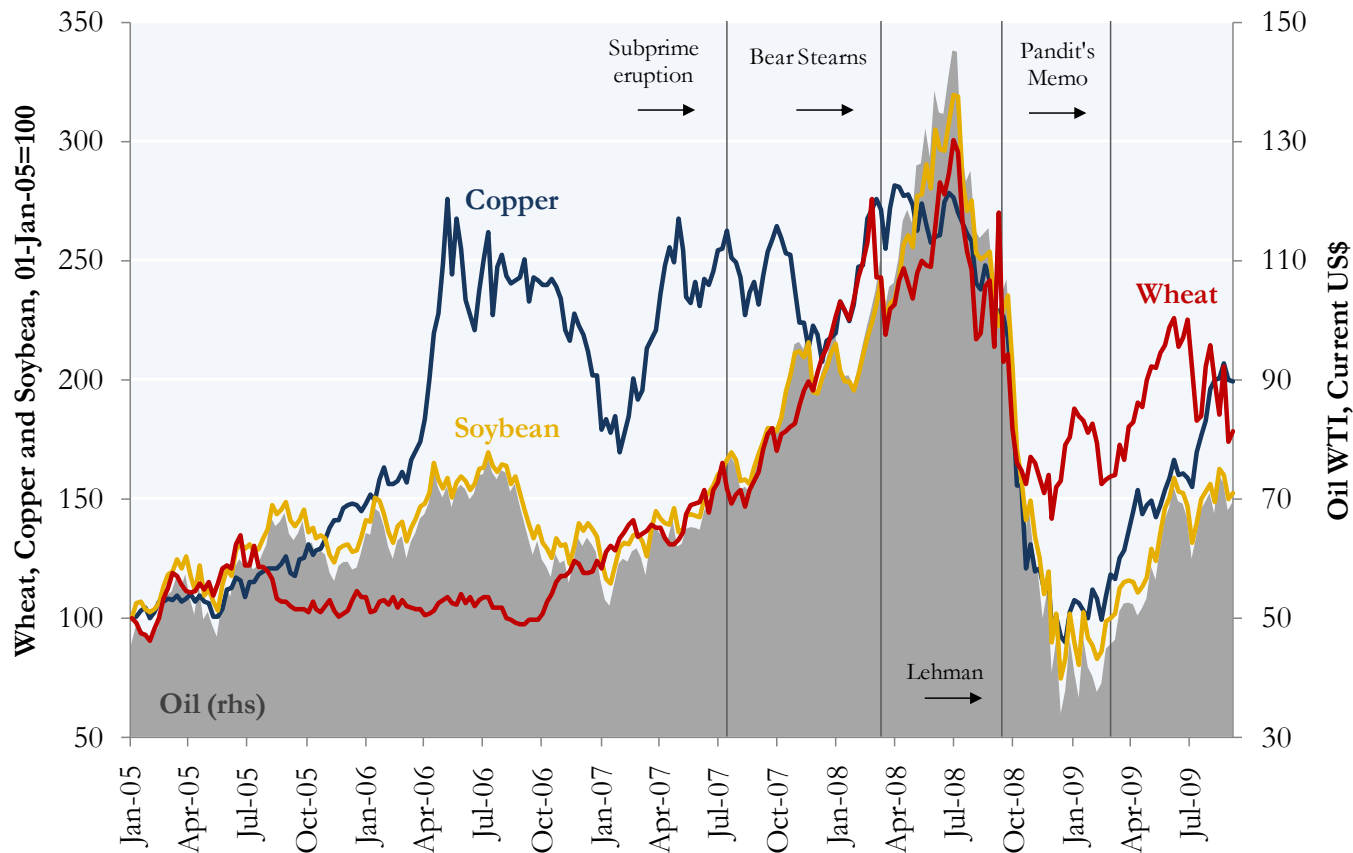
Corporate EMBI & U.S. High Yield Bond Spread
in basis points



And the rebound in commodity prices benefit net exporting countries in the region

Commodity Prices

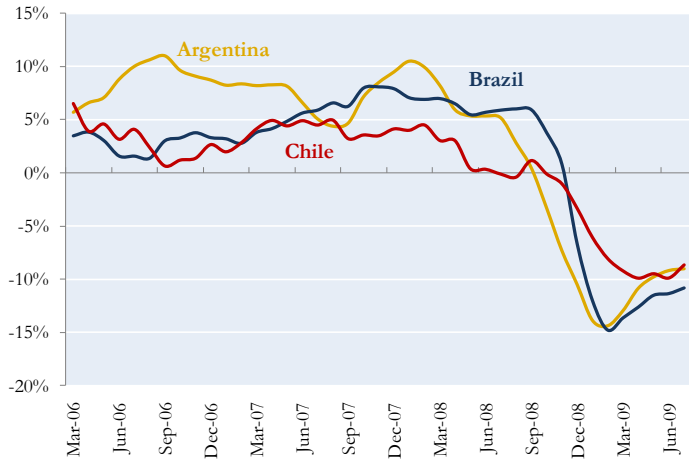
Oil WTI in Current US\$, Wheat, Copper and Soybean: Index 01-Jan-05=100



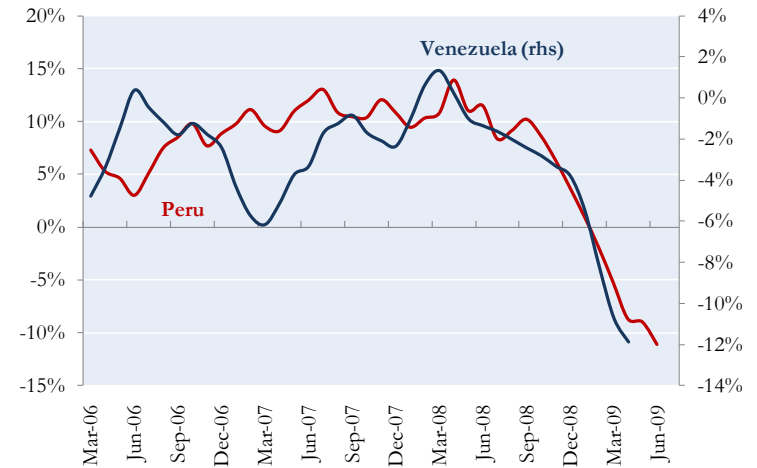
- About 95% of LAC's GDP and 90% of LAC's population reside in countries that are net commodity exporters
- About half the number of countries in LAC are net commodity importers and are mainly located in Central America and the Caribbean

There is considerable heterogeneity in the pace of recovery across LAC countries

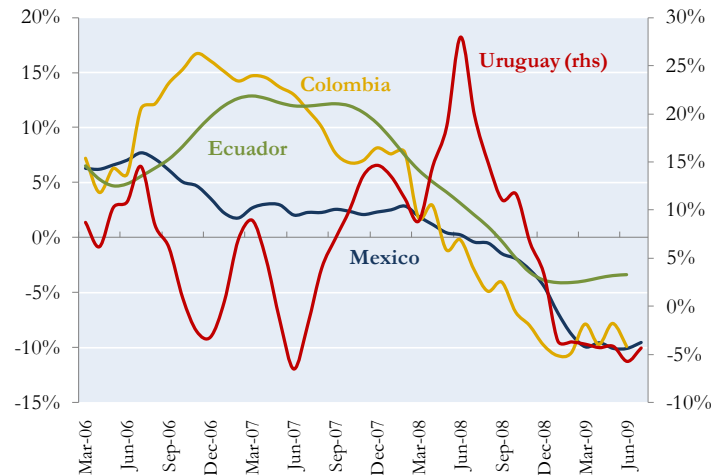
Rebounding



Still Falling



Stabilized?

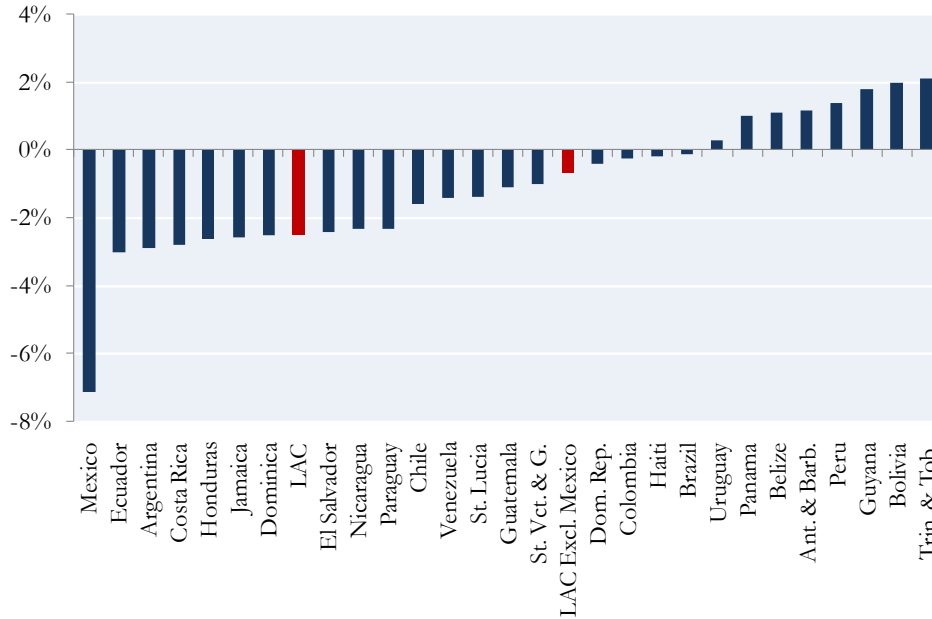


How Has LAC Fared in Comparative Terms?

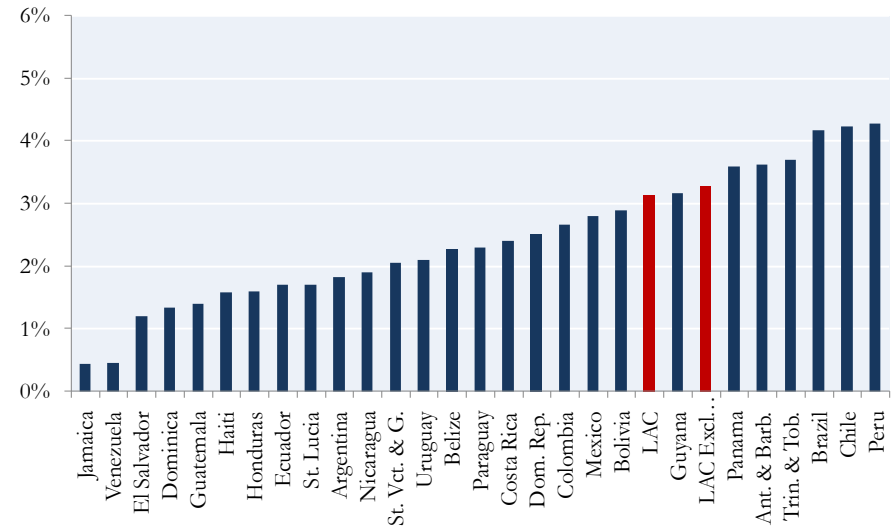
Part 2

2009 will be a year of recession for LAC (Mexico the hardest hit) but a broad recovery is expected for 2010

2009 Real GDP Growth Forecast

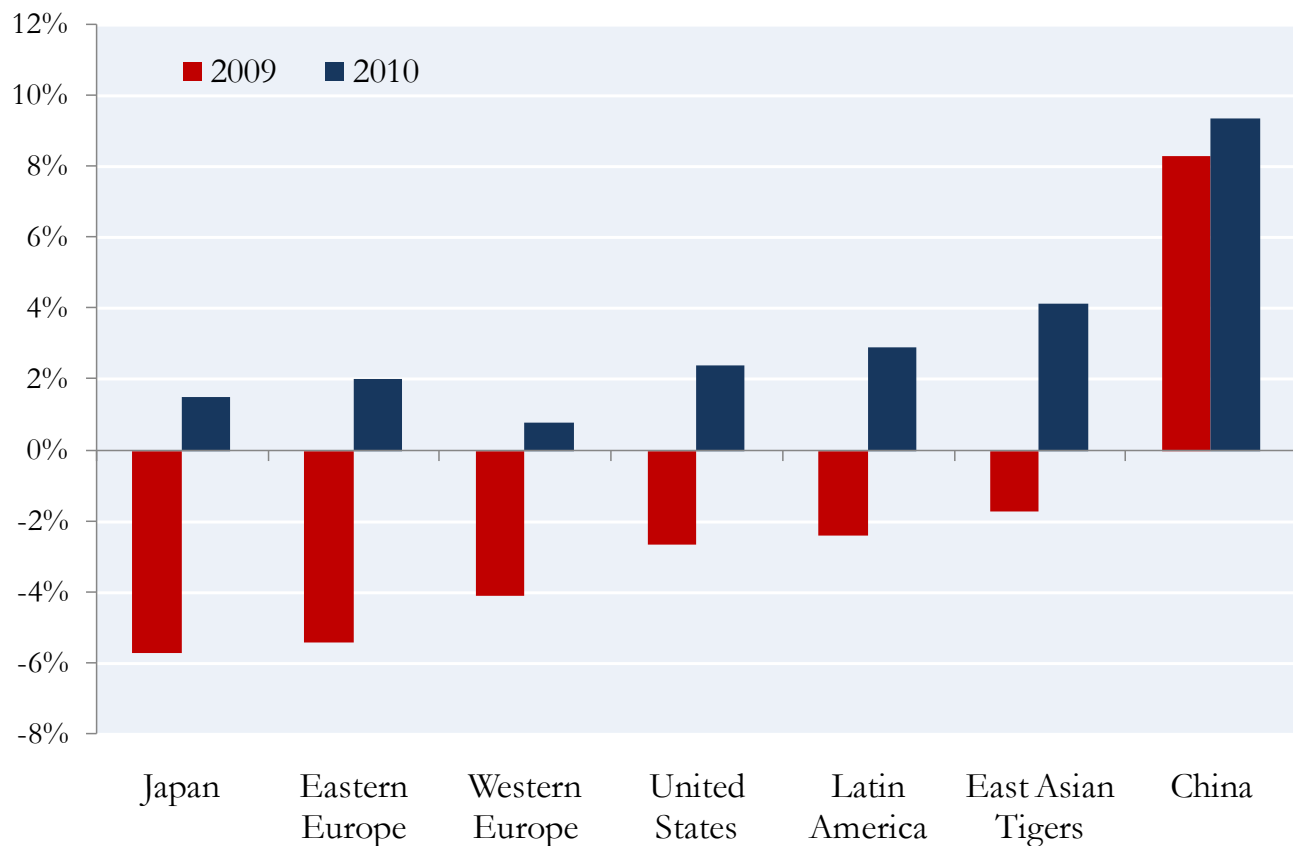


2010 Real GDP Growth Forecast

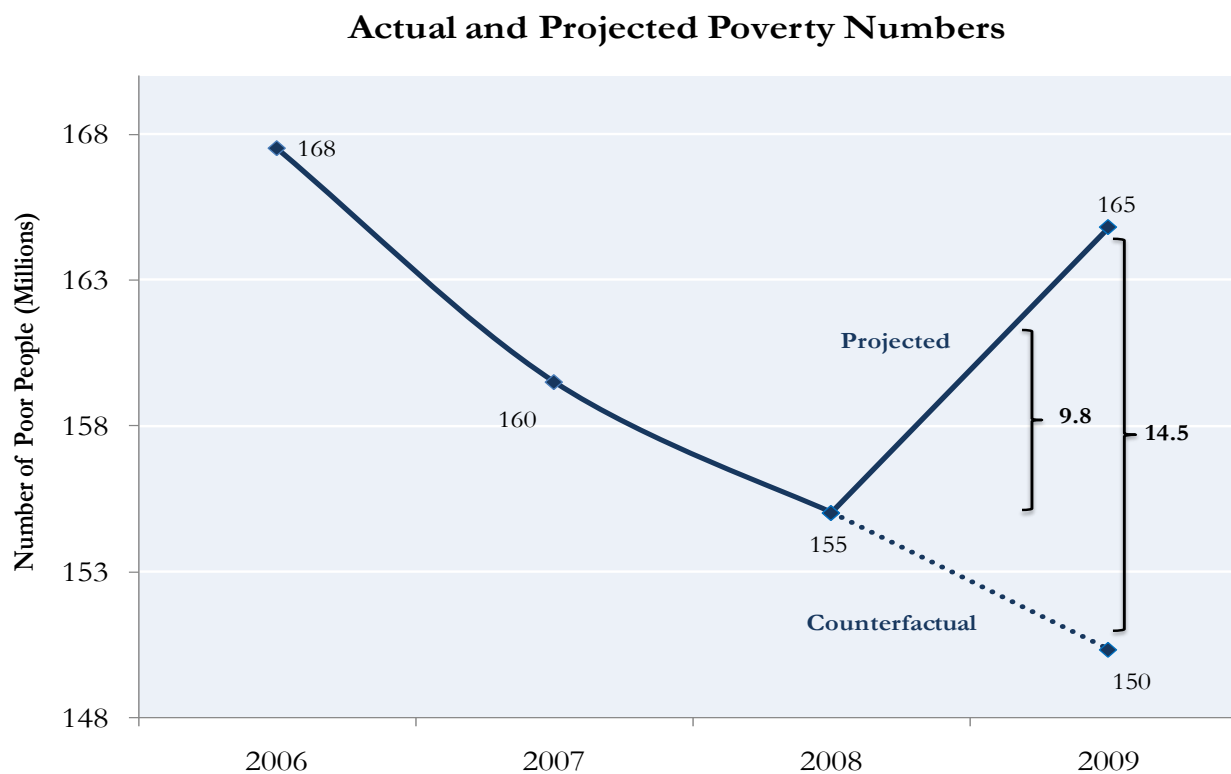


The 2009 recession in LAC is less pronounced than in other areas of the world

Recent Real GDP Growth and Forecasts for 2009-2010
Annual GDP Real Growth Rate,

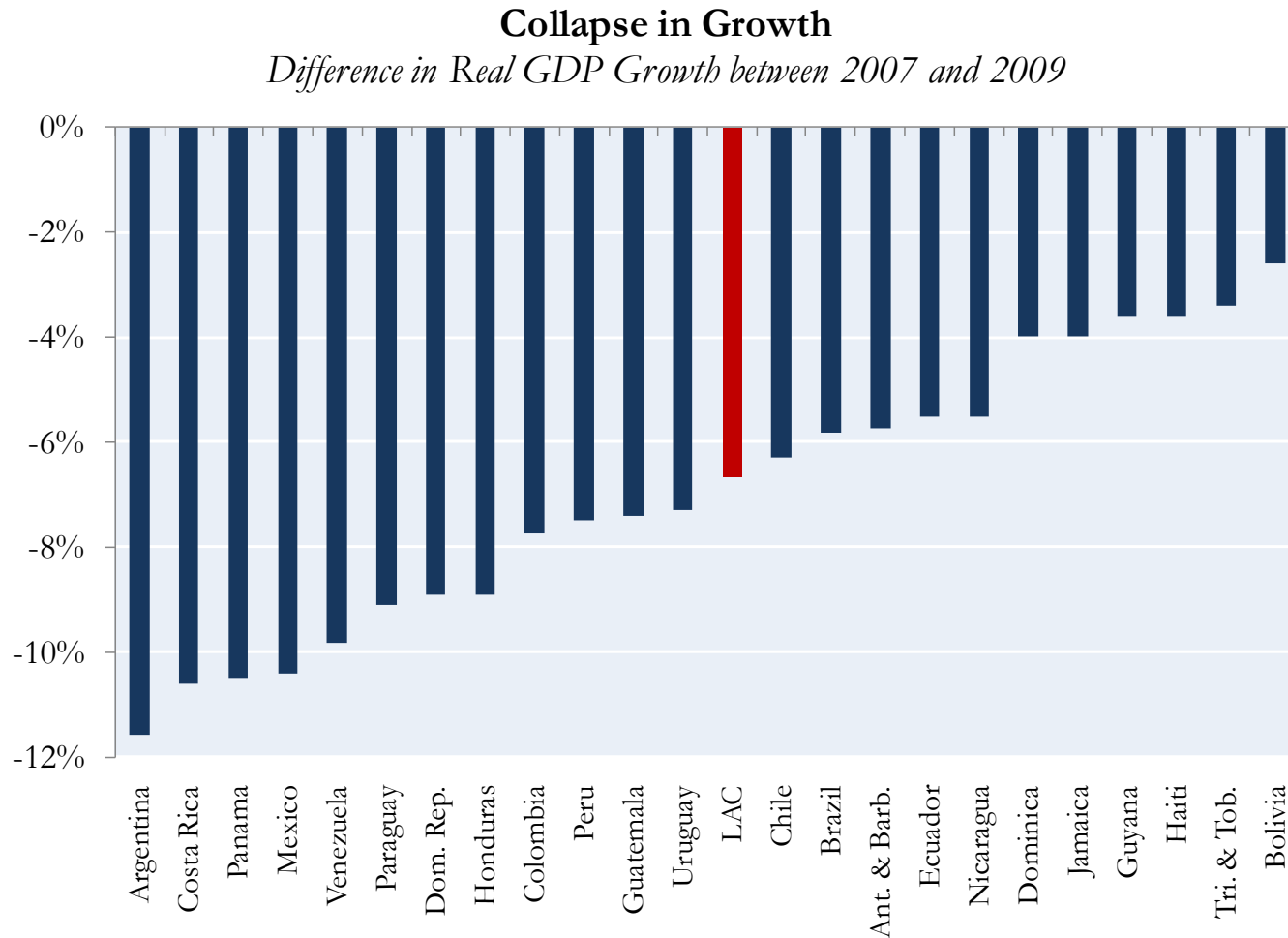


But the recession in LAC threatens social gains



- *Between 2002 and 2008, almost 60 million people in LAC moved out of poverty.*

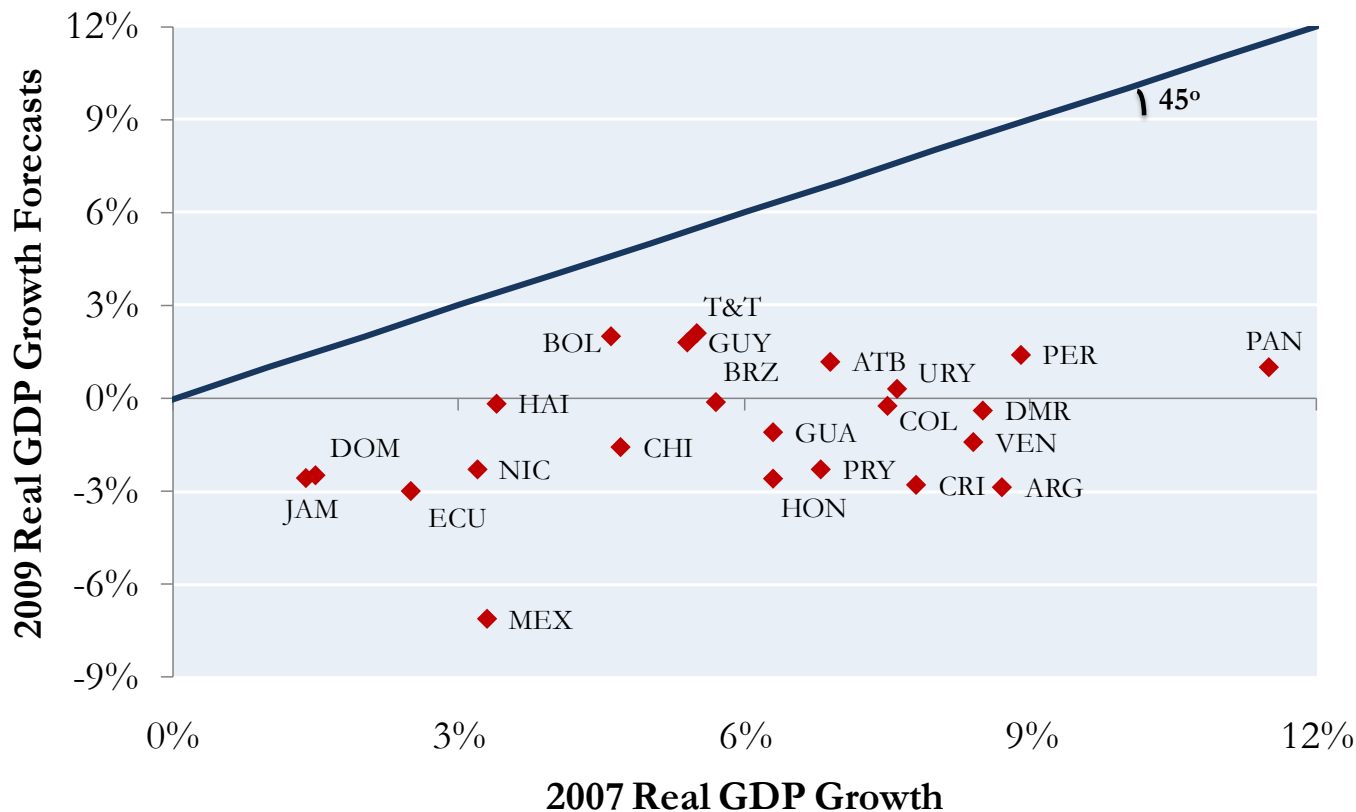
The *growth collapse* in LAC is significant on average, although cross-country variation is non-trivial



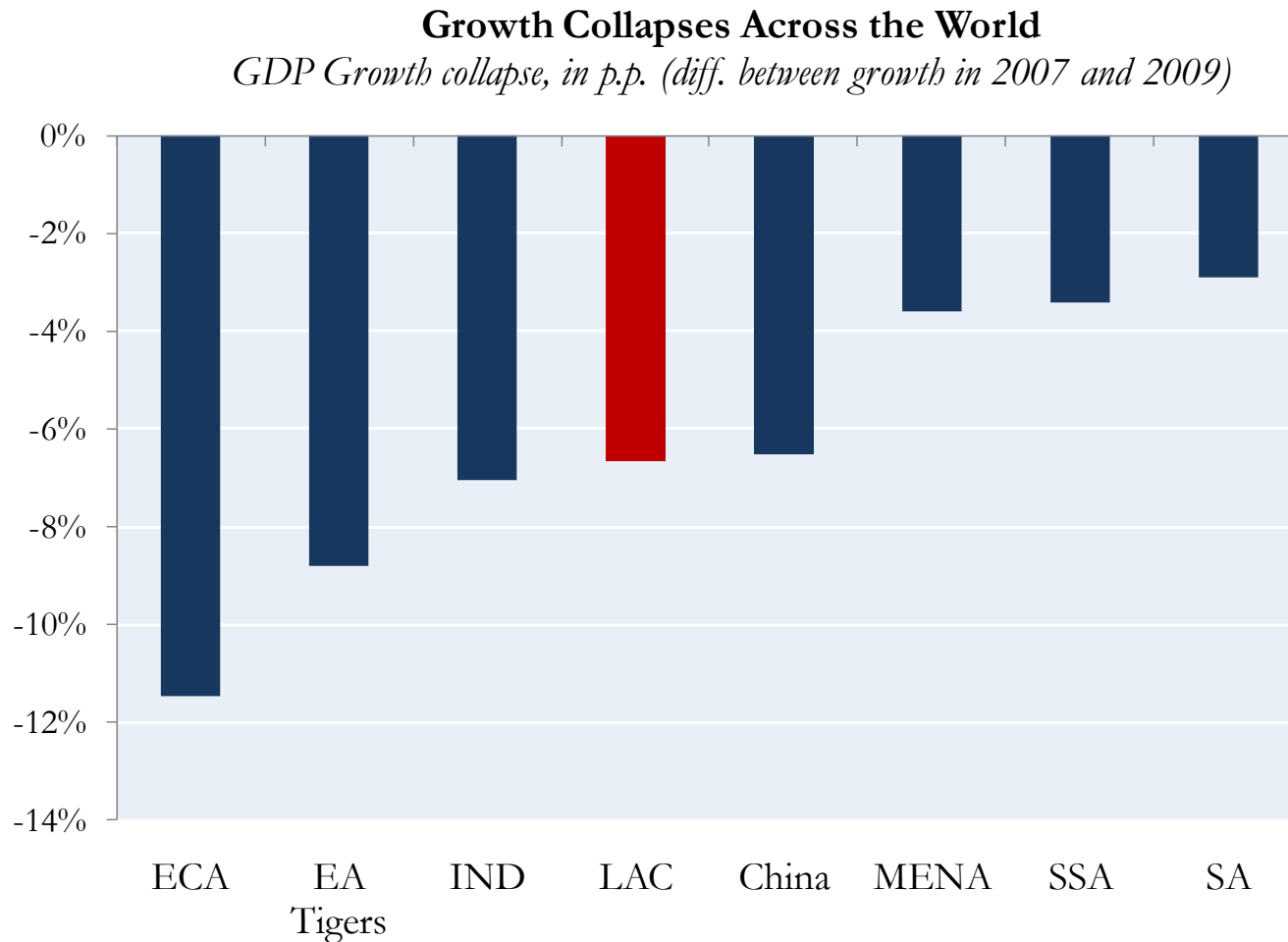
For many LAC countries, the collapse was from relatively high growth rates

Real GDP Growth in LAC

2007 and 2009 Forecasts



LAC's growth collapse is similar to China's and smaller to that of the Tigers and Eastern Europe

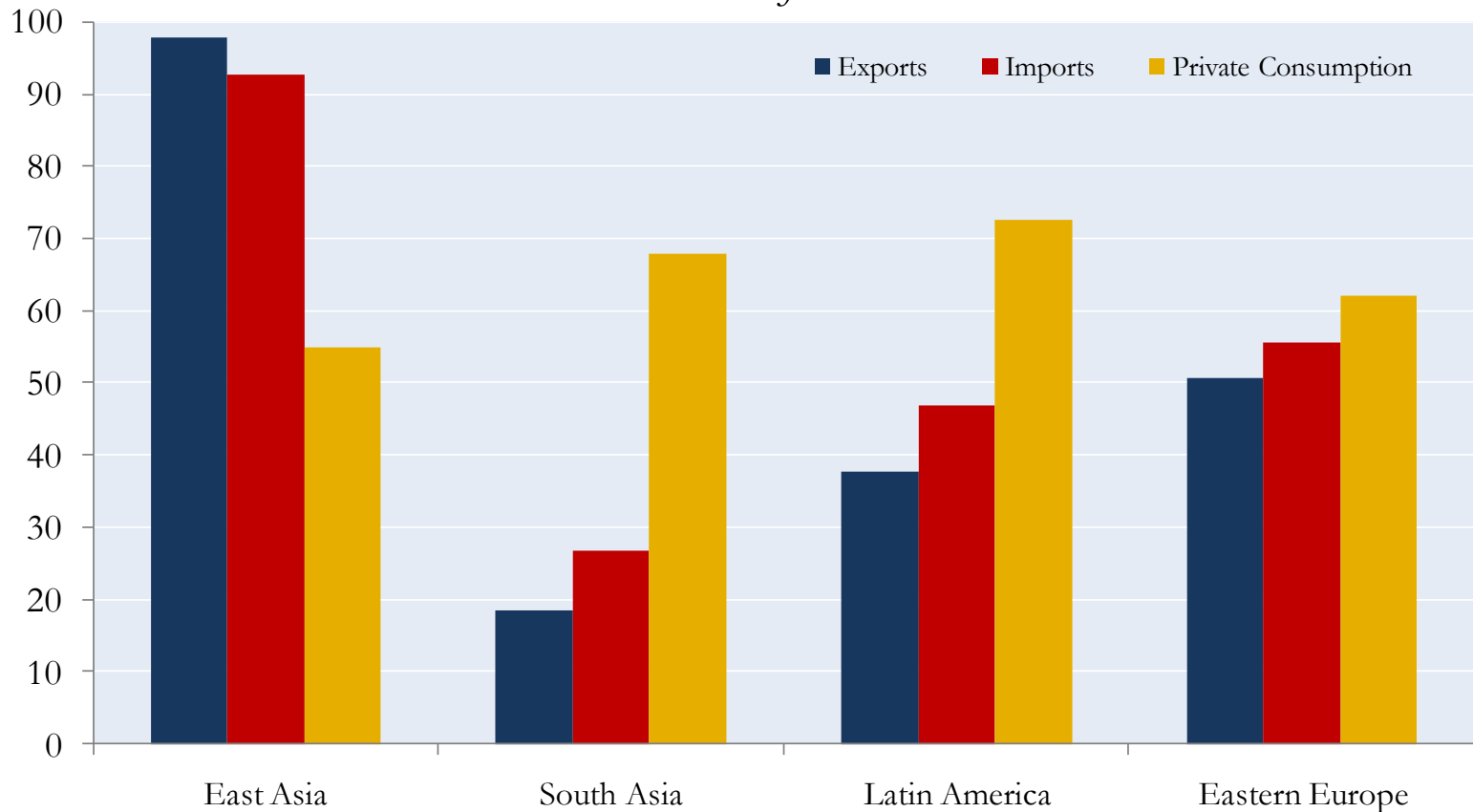


Explaining cross-country differences in the collapse

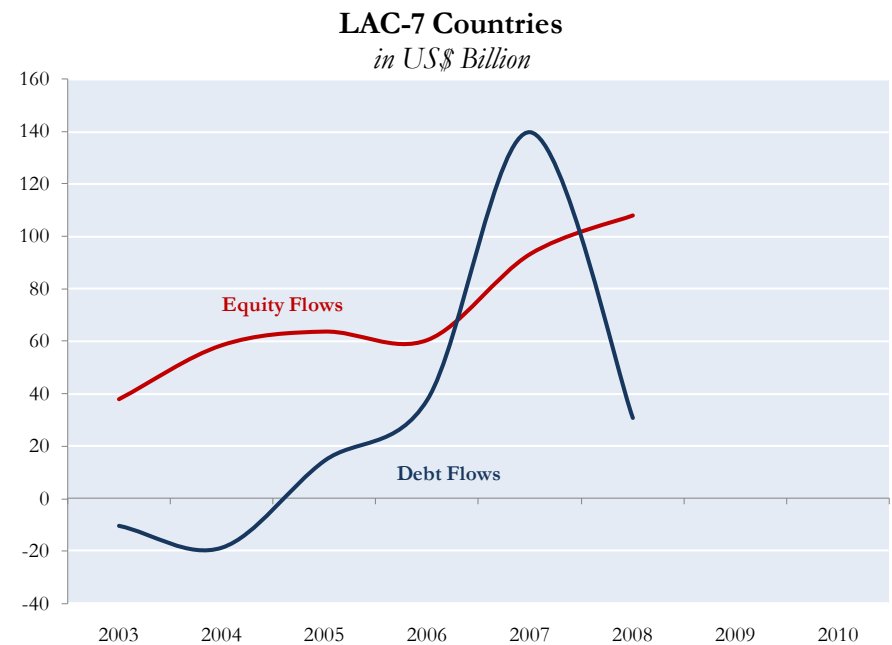
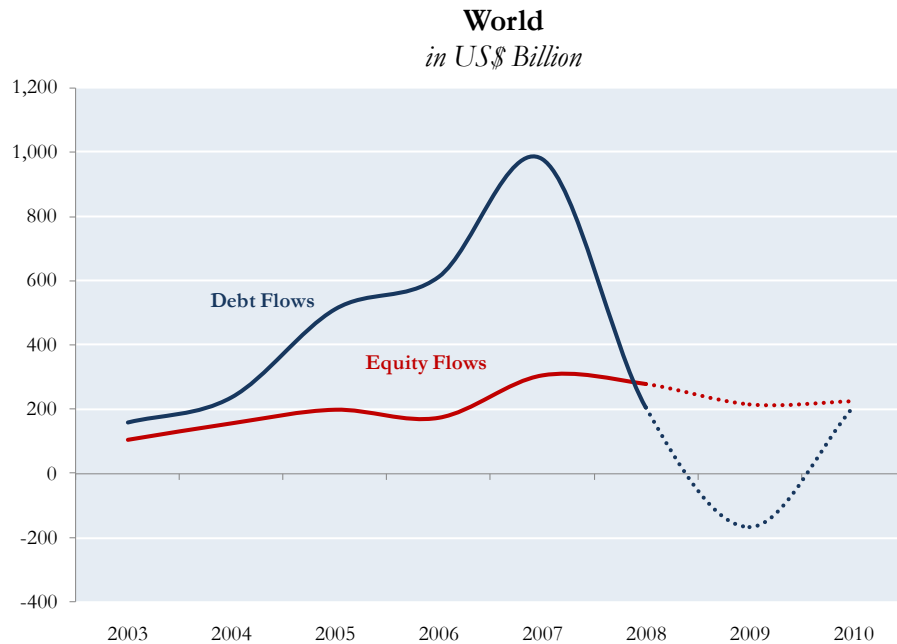
- Regression analysis of the growth collapse from 2007 to 2009
 - Sample of 126 countries
- Collapses were larger in countries characterized by
 - Greater trade and financial openness
 - Higher share of manufacturing exports
 - Greater export reliance on rich country markets
 - Weaker banking systems
- This helps explain contrasts in the collapse
 - Brazil-Mexico; LAC-Eastern Europe; LAC-East Asian Tigers
- Soundness of macro policies played a positive role
 - Dampening the collapse somewhat
 - Enabling countercyclical policies, particularly in the monetary front
 - Helping avoid systemic damage

Trade openness across emerging regions

Structure of GDP *as % of GDP*

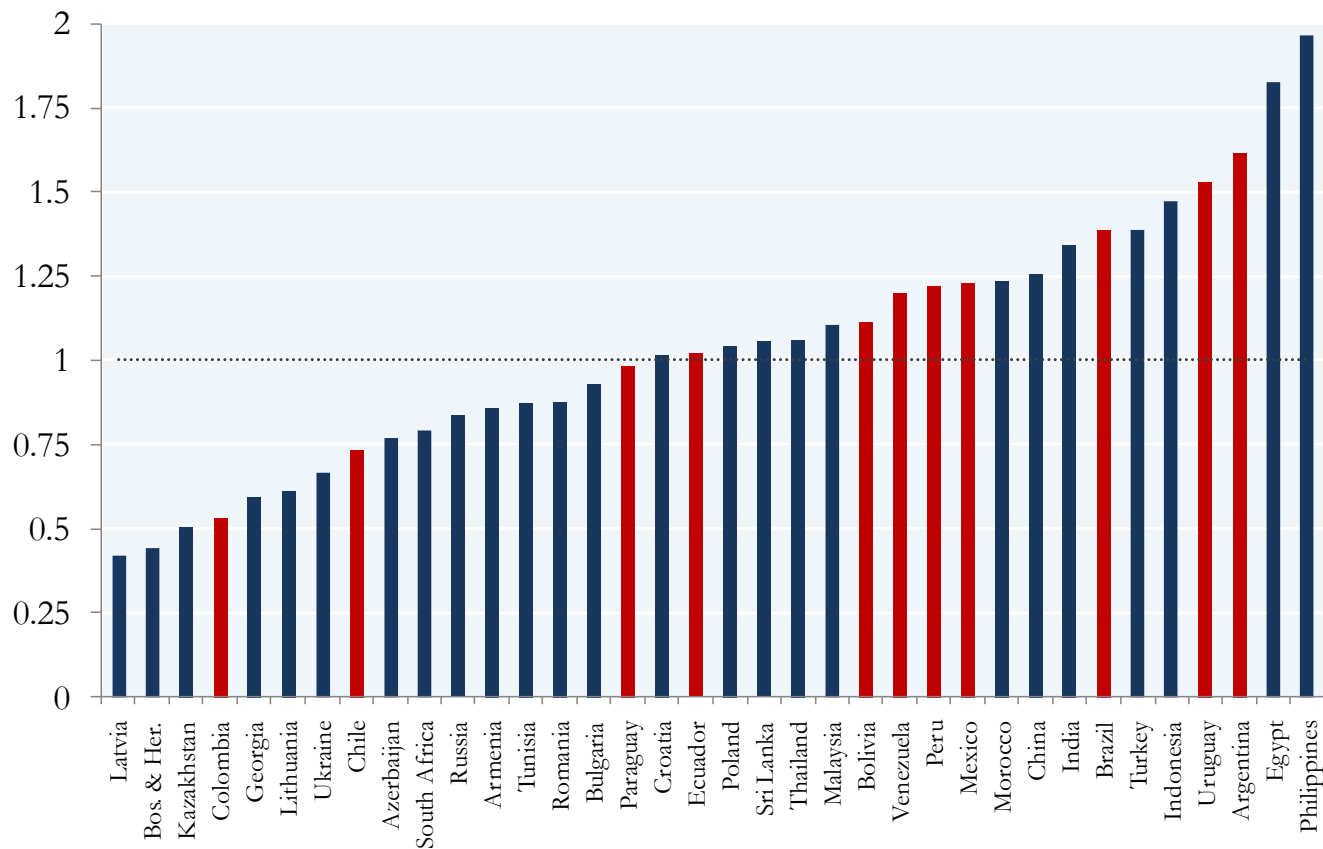


The fall in foreign debt flows stands in sharp contrast with the stability of equity flows



Healthy banking systems dampened the collapse

Deposit to Loan Ratios
Emerging Countries, 2007 Data



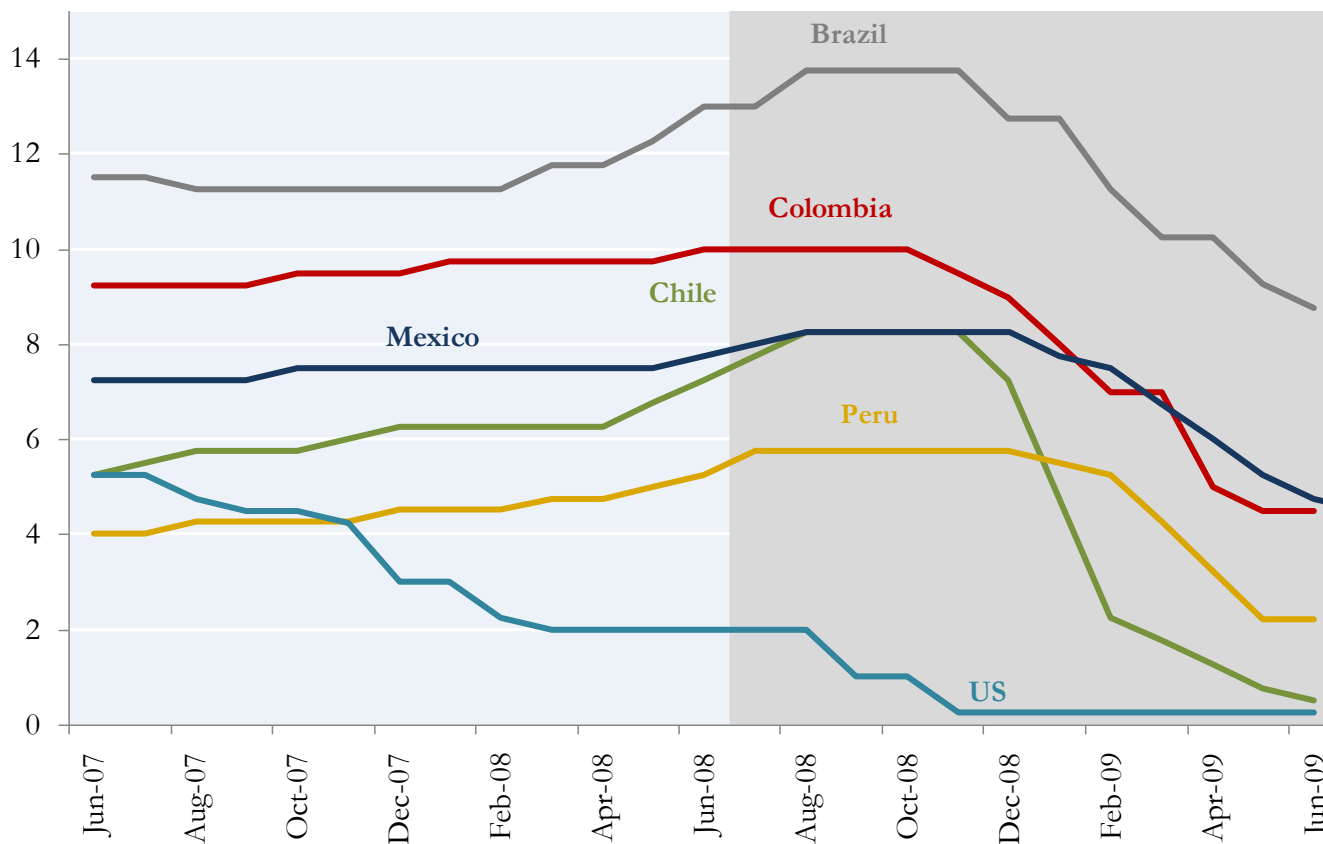
The dog that did not bark: absence of domestic crises in a region traditionally plagued by them

Banking Crises in LAC Countries

1980-1985		1995-2000		2008-2009	
Argentina	1980	Argentina	1995		
Brazil	1985	Brazil	1995		
Chile	1980	Colombia	1998		
Colombia	1982	Ecuador	1996, 1998		
Ecuador	1980	Honduras	1999		
Mexico	1981	Jamaica	1996		
Peru	1983	Nicaragua	2000		
Uruguay	1981	Paraguay	1995		
		Peru	1999		

Inflation-targeting countries in LAC undertook aggressive countercyclical monetary policies

Monetary Policy Rates
Inflation-Targeting LAC Countries, in %



Looking Ahead: Much Haziness in the Horizon

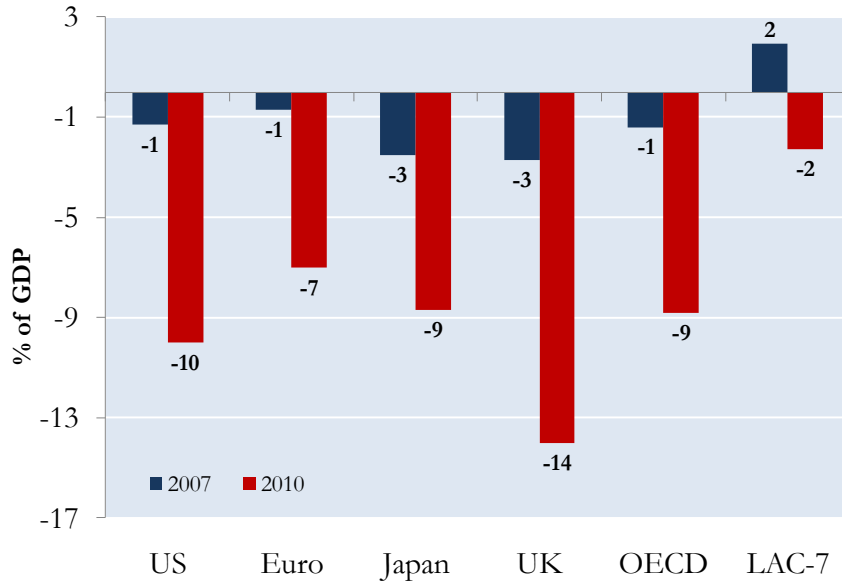
Part 3

By and large, LAC is well-positioned for recovery

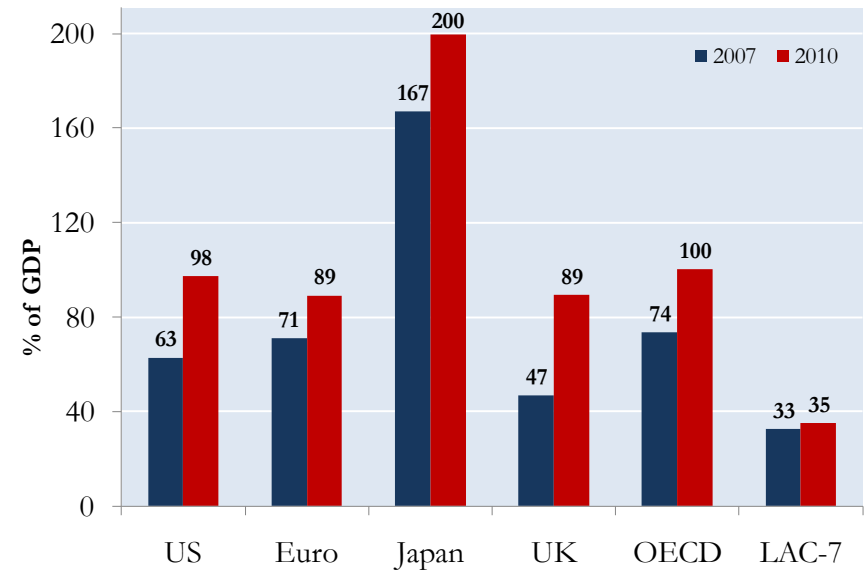
- Despite being financially globalized, LAC is coming out of the crisis without systemic damage
 - Improved macro-financial immune system passed a tough test
 - In contrast with rich countries, LAC's fiscal and debt positions remain comfortable
 - Exchange rate flexibility acted as cushion (countercyclicality) and facilitated external adjustment at lower output cost than otherwise
 - LAC economies that are complementary to China's lead the recovery
- Thus, LAC emerging as an attractive destination for investment
- But LAC will need to intensify its productivity-oriented agenda to seize opportunities going forward
 - Keeping the course of improvement in social and macrofinancial policy

Unlike rich countries, LAC comes out of the crisis with comfortable fiscal & public debt positions

Fiscal Balance

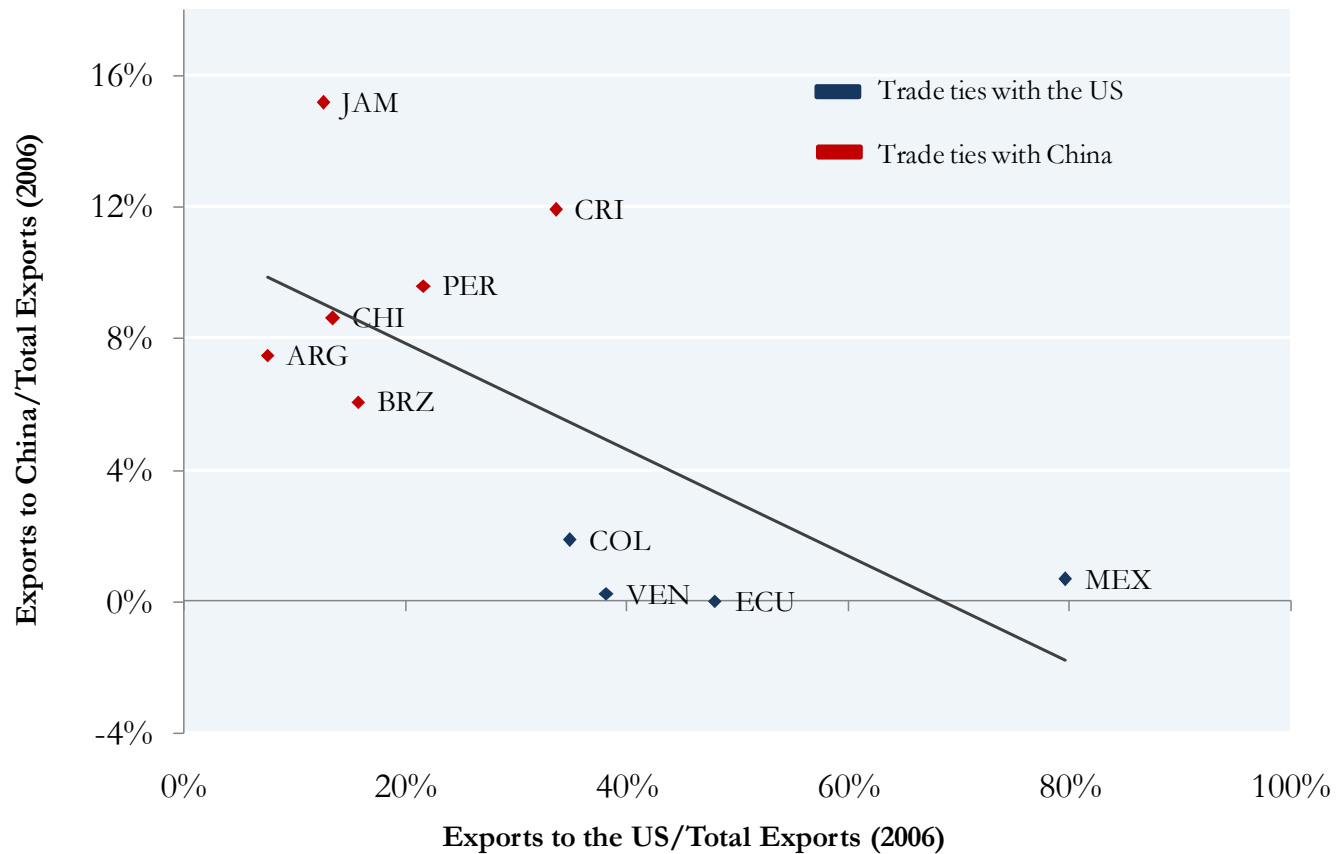


Gross Nominal Liabilities



LAC economies that are complementary to China's are recovering first

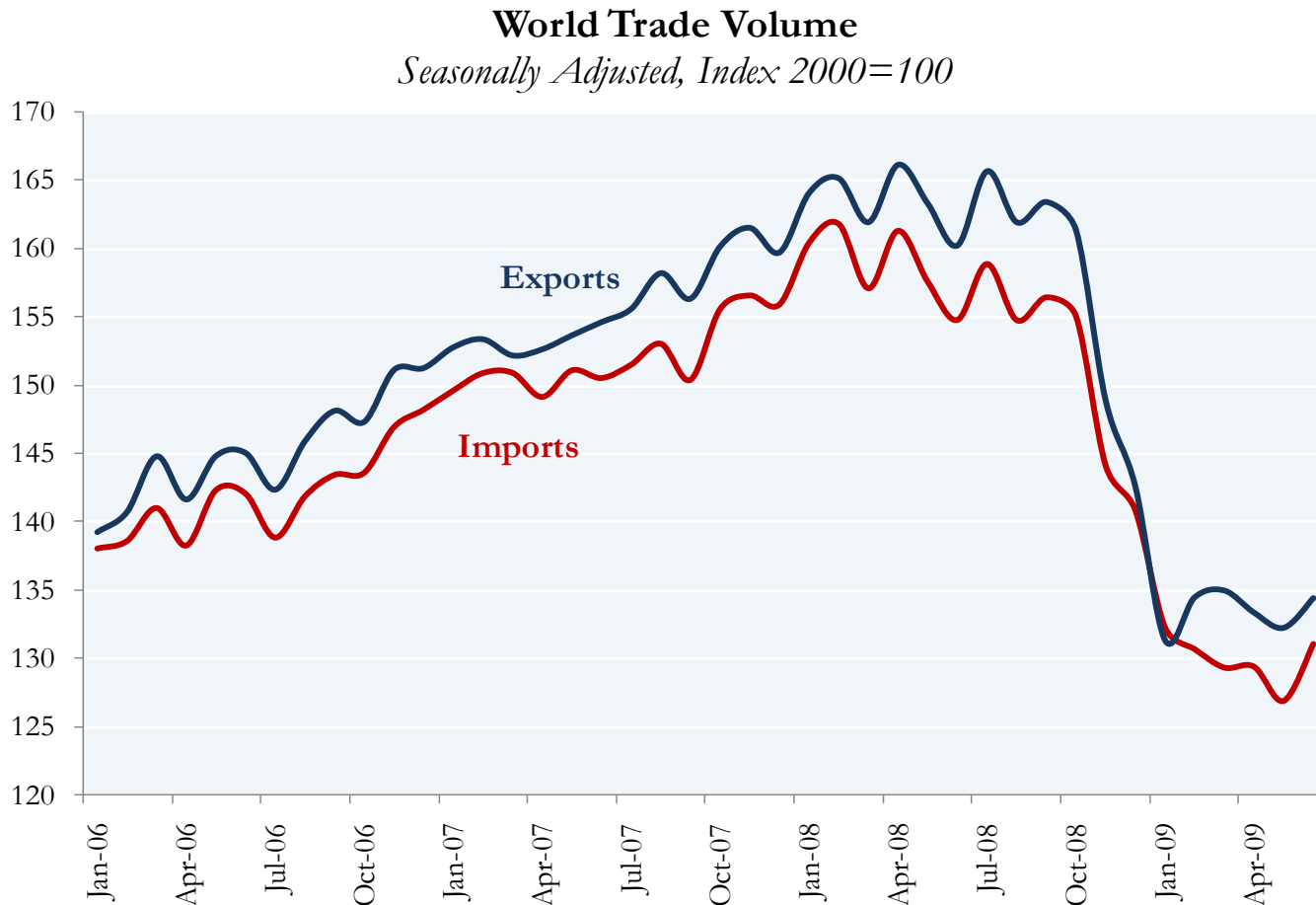
Trade ties with the US and China



LAC prospects depend on world growth, where much haziness exist beyond the short run

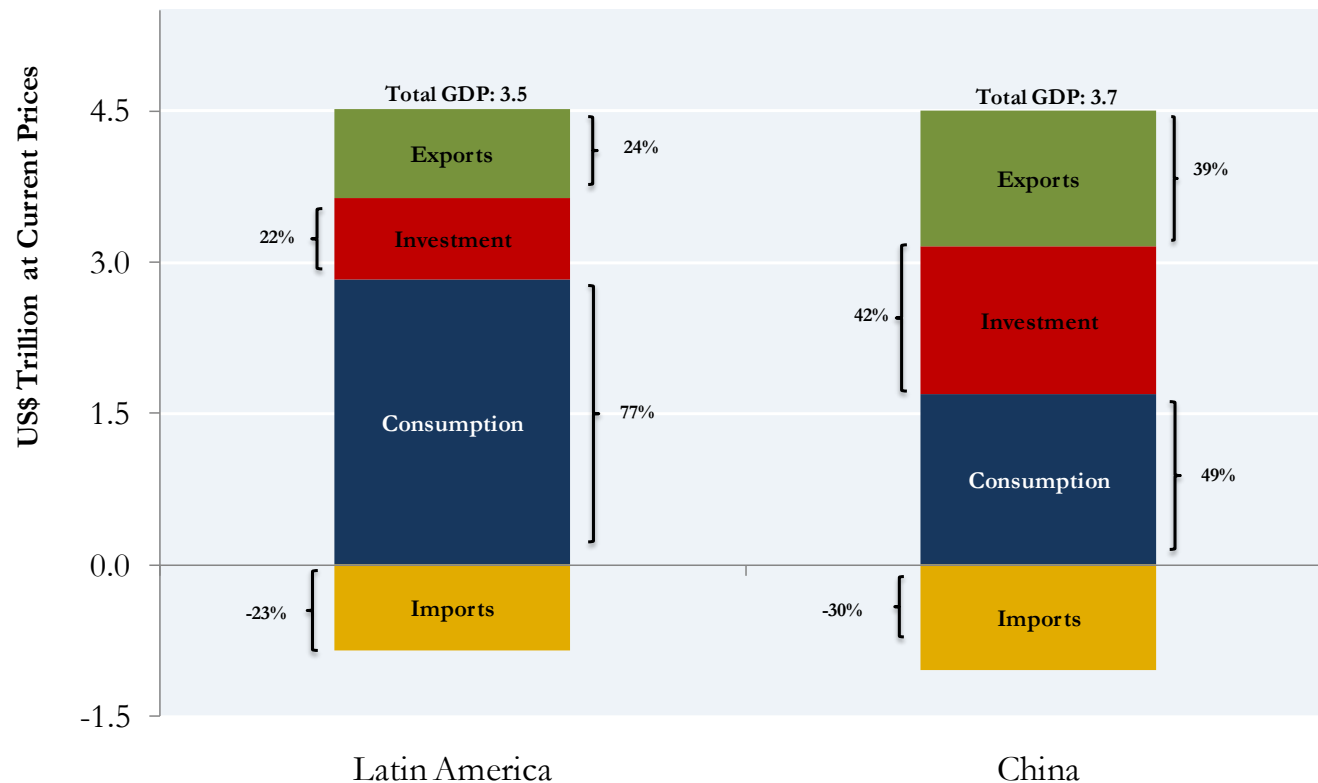
- In the short run, the global recovery is looking a lot like a V...
- ...but economic repair is still incomplete and fragilities remain
 - Will private sector demand be strong when stimulus fizzles away?
 - Will exit from stimulus policies be well-timed and orderly?
 - Premature retreat can kill the recovery; delayed retreat can rise inflation specter
- Medium-term growth for the world might be subdued
 - Financial system still impaired
 - Scenario of slow expansion of world trade in the context of rebalancing
 - Possible adverse impact on MT investment of regulatory uncertainty
- LAC can grow robustly while contributing to global rebalancing
 - LAC economy is the size of China's but consumption has greater weight and investment has significant room to expand

World trade volume unlikely to grow fast for a while in a context of global rebalancing



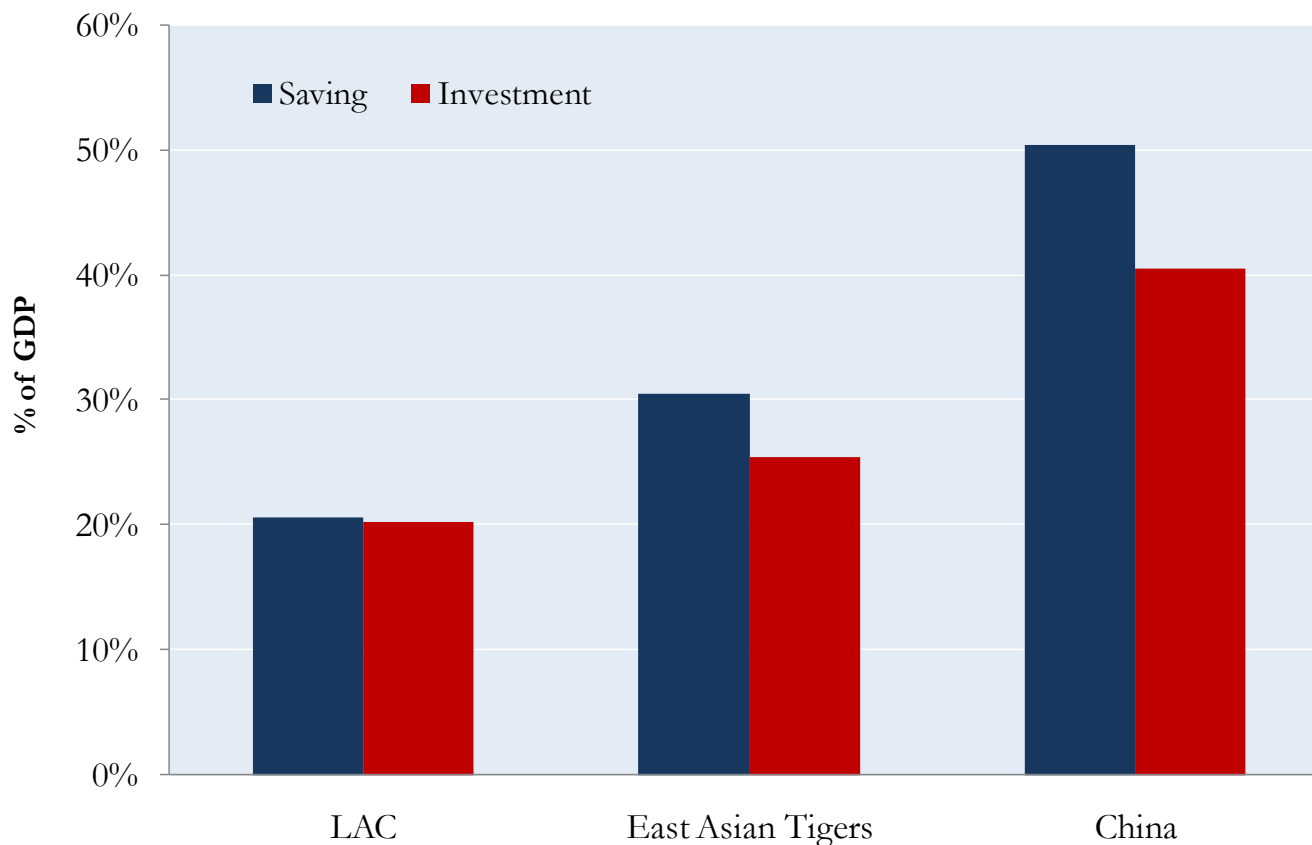
At the margin, LAC can contribute to global rebalancing more than China...

Output and Demand: China vs. LAC
GDP and Demand Components, 2007



... while raising savings and investment rates to underpin a higher growth path

Savings and Investment
Average Between 2006-2008



Thank you